Willis

August 31, 2005

Website: www.willis.com

Direct Line: (312) 621-4806
Direct Fax: (312) 621-6875
E-mail: john.johnson@willis.com

Arizona Department of Environmental Quality
Contracts and Procurement Section
1110 West Washington Street
Phoenix, Arizona 85007-2953

**Re:** MACTEC Engineering and Consulting, Inc.

**Subject:** **Assessment and Remediation of Pollutants**

Dear Sir or Madam,

MACTEC Engineering and Consulting, Inc. has been extended a bonding facility to support projects up to $10 million. Surety bonds are issued through The Insurance Company of the State of Pennsylvania. The Insurance Company of the State of Pennsylvania is rated A++ XV by A.M. Best and is listed in the Federal Register, as well, licensed to do business in the State of Arizona.

We heartily endorse their organization and feel you would find them to be the most qualified to undertake and successfully complete your anticipated project and we will provide the requisite bonding should the project be awarded to MACTEC Engineering and Consulting, Inc. This bonding program is subject to acceptable contractual and underwriting terms and conditions.

If we can provide any further assistance, please do not hesitate to call upon us.

Sincerely,

The Insurance Company of the State of Pennsylvania
John K. Johnson, Attorney-In-Fact

JKJ/rc

**Willis of Illinois, Inc.**
John K. Johnson
10 S. LaSalle Street
Suite 3000
Chicago, Illinois 60603

**The Insurance Company of the State of Pennsylvania**
Principal Bond Office: 70 Pine Street, New York, N.Y. 10270

# POWER OF ATTORNEY

No. 02-B-03531

**KNOW ALL MEN BY THESE PRESENTS:**

That The Insurance Company of the State of Pennsylvania, a Pennsylvania corporation, does hereby appoint

**--- Patricia M. Stein, Marcia A. Ritter, Adrienne C. Stevenson, John K. Johnson, Samuel L. Ware, Jr. , Candace T. Stevenson: of Chicago, Illinois---**

its true and lawful Attorney(s)-in-Fact, with full authority to execute on its behalf bonds, undertakings, recognizances and other contracts of indemnity and writings obligatory in the nature thereof, issued in the course of its business, and to bind the company thereby.

**IN WITNESS WHEREOF**, The Insurance Company of the State of Pennsylvania has executed these presents

this 3rd day of March, 2003

Michael C. Fay

Michael C. Fay, Vice President

**STATE OF NEW YORK }**
**COUNTY OF NEW YORK}ss.**

On this 3rd day of March 2003 before me came the above named officer of The Insurance Company of the State of Pennsylvania, to me personally known to be the individual and officer described herein, and acknowledged that he executed the foregoing instrument and affixed the seal of said corporation thereto by authority of his office.

Dorothy L. Parker

DOROTHY L. PARKER
Notary Public, State of New York
No. 01PA6060631
Qualified in Richmond County
Commission Expires June 25, 03

## CERTIFICATE

Excerpts of Resolution adopted by the Board of Directors of The Insurance Company of the State of Pennsylvania, on May 18, 1976:

"**RESOLVED,** that the Chairman of the Board, the President, or any Vice President be, and hereby is, authorized to appoint Attorneys-in-Fact to represent and act for and on behalf of the Company to execute bonds, undertakings, recognizances and other contracts of indemnity and writings obligatory in the nature thereof, and to attach thereto the corporate seal of the Company, in the transaction of its surety business;

"**RESOLVED,** that the signatures and attestations of such officers and the seal of the Company may be affixed to any such Power of Attorney or to any certificate relating thereto by facsimile, and any such Power of Attorney or certificate bearing such facsimile signatures or facsimile seal shall be valid and binding upon the Company when so affixed with respect to any bond, undertaking, recognizance or other contract of indemnity or writing obligatory in the nature thereof;

"**RESOLVED**, that any such Attorney-in-Fact delivering a secretarial certification that the foregoing resolutions still be in effect may insert in such certification the date thereof, said date to be not later than the date of delivery thereof by such Attorney-in-Fact."

I, Elizabeth M. Tuck, Secretary of The Insurance Company of the State of Pennsylvania, do hereby certify that the foregoing excerpts of Resolution adopted by the Board of Directors of this corporation, and the Power of Attorney issued pursuant thereto, are true and correct, and that both the Resolution and the Power of Attorney are in full force and effect.

**IN WITNESS WHEREOF**, I have hereunto set my hand and affixed the facsimile seal of the corporation

this 31st day of August, 2005

Elizabeth M. Tuck

Elizabeth M. Tuck, Secretary

23238 (4/99)

**MARSH**

# CERTIFICATE OF INSURANCE

**CERTIFICATE NUMBER**
SEA-000804129-01

**PRODUCER**
MARSH USA INC.
1225 17TH STREET, SUITE 2100
DENVER, CO 80202-5534
Attn: Steve Wilson 303-308-4569

J59009-E&O-M-ALL-2002

**THIS CERTIFICATE IS ISSUED AS A MATTER OF INFORMATION ONLY AND CONFERS NO RIGHTS UPON THE CERTIFICATE HOLDER OTHER THAN THOSE PROVIDED IN THE POLICY. THIS CERTIFICATE DOES NOT AMEND, EXTEND OR ALTER THE COVERAGE AFFORDED BY THE POLICIES DESCRIBED HEREIN.**

**COMPANIES AFFORDING COVERAGE**

| COMPANY | |
|---|---|
| A | ZURICH AMERICAN INSURANCE COMPANY |
| B | STEADFAST INSURANCE COMPANY |
| C | AMERICAN INTERNATIONAL SPECIALTY LINES INS. CO. |
| D | |

**INSURED**
MACTEC ENGINEERING AND CONSULTING, INC.
1105 SANCTUARY PARKWAY, SUITE 300
PHONE: (770) 360-0600
ALPHARETTA, GA 30004

## COVERAGES

THIS IS TO CERTIFY THAT POLICIES OF INSURANCE DESCRIBED HEREIN HAVE BEEN ISSUED TO THE INSURED NAMED HEREIN FOR THE POLICY PERIOD INDICATED. NOTWITHSTANDING ANY REQUIREMENT, TERM OR CONDITION OF ANY CONTRACT OR OTHER DOCUMENT WITH RESPECT TO WHICH THE CERTIFICATE MAY BE ISSUED OR MAY PERTAIN, THE INSURANCE AFFORDED BY THE POLICIES DESCRIBED HEREIN IS SUBJECT TO ALL THE TERMS, CONDITIONS AND EXCLUSIONS OF SUCH POLICIES. AGGREGATE LIMITS SHOWN MAY HAVE BEEN REDUCED BY PAID CLAIMS.

| CO LTR | TYPE OF INSURANCE | POLICY NUMBER | POLICY EFFECTIVE DATE (MM/DD/YY) | POLICY EXPIRATION DATE (MM/DD/YY) | LIMITS | |
|---|---|---|---|---|---|---|
| | **GENERAL LIABILITY** | | | | GENERAL AGGREGATE | $ 2,000,000 |
| A | X COMMERCIAL GENERAL LIABILITY | GLO 225862807 | 09/01/04 | 09/01/05 | PRODUCTS - COMP/OP AGG | $ 2,000,000 |
| | CLAIMS MADE  X OCCUR | | | | PERSONAL & ADV INJURY | $ 1,000,000 |
| | OWNER'S & CONTRACTOR'S PROT | | | | EACH OCCURRENCE | $ 1,000,000 |
| | | | | | FIRE DAMAGE (Any one fire) | $ 250,000 |
| | | | | | MED EXP (Any one person) | $ 5,000 |
| | **AUTOMOBILE LIABILITY** | | | | COMBINED SINGLE LIMIT | $ 1,000,000 |
| A | X ANY AUTO | BAP 225862907 (AOS) | 09/01/04 | 09/01/05 | | |
| A | ALL OWNED AUTOS | TAP 283353907 (TX) | 09/01/04 | 09/01/05 | BODILY INJURY (Per person) | $ |
| | SCHEDULED AUTOS | | | | | |
| | X HIRED AUTOS | | | | BODILY INJURY (Per accident) | $ |
| | X NON-OWNED AUTOS | | | | | |
| | | | | | PROPERTY DAMAGE | $ |
| | **GARAGE LIABILITY** | | | | AUTO ONLY - EA ACCIDENT | $ |
| | ANY AUTO | | | | OTHER THAN AUTO ONLY: | |
| | | | | | EACH ACCIDENT | $ |
| | | | | | AGGREGATE | $ |
| | **EXCESS LIABILITY** | | | | EACH OCCURRENCE | $ 5,000,000 |
| B | X UMBRELLA FORM | SUO 525751502 | 09/01/04 | 09/01/05 | AGGREGATE | $ 5,000,000 |
| | OTHER THAN UMBRELLA FORM | | | | | $ |
| | **WORKERS COMPENSATION AND EMPLOYERS' LIABILITY** | | | | X WC STATUTORY LIMITS  OTHER | |
| A | | WC 225863007 (AOS) | 09/01/04 | 09/01/05 | EL EACH ACCIDENT | $ 1,000,000 |
| A | THE PROPRIETOR/ PARTNERS/EXECUTIVE OFFICERS ARE: X INCL  EXCL | WC 283354007 (WI) & (MA) | 09/01/04 | 09/01/05 | EL DISEASE-POLICY LIMIT | $ 1,000,000 |
| | | | | | EL DISEASE-EACH EMPLOYEE | $ 1,000,000 |
| | **OTHER** | | | | | |
| B | POLLUTION LIABILITY | CPL 682080712 | 09/01/04 | 09/01/05 | $1,000,000 EACH CLAIM/AGG. | |
| C | PROFESSIONAL LIABILITY | 1952560 | 09/01/04 | 09/01/05 | $1,000,000 EACH CLAIM/AGG. | |

**DESCRIPTION OF OPERATIONS/LOCATIONS/VEHICLES/SPECIAL ITEMS**

## CERTIFICATE HOLDER

EVIDENCE OF INSURANCE

## CANCELLATION

SHOULD ANY OF THE POLICIES DESCRIBED HEREIN BE CANCELLED BEFORE THE EXPIRATION DATE THEREOF, THE INSURER AFFORDING COVERAGE WILL ENDEAVOR TO MAIL 30 DAYS WRITTEN NOTICE TO THE CERTIFICATE HOLDER NAMED HEREIN, BUT FAILURE TO MAIL SUCH NOTICE SHALL IMPOSE NO OBLIGATION OR LIABILITY OF ANY KIND UPON THE INSURER AFFORDING COVERAGE, ITS AGENTS OR REPRESENTATIVES, OR THE ISSUER OF THIS CERTIFICATE.

**MARSH USA INC.**
BY: Dorothy A. Stevens  Dorothy A. Stevens

MM1(3/02)

**VALID AS OF:** 09/01/04

# MACTEC, Inc.
**Consolidated Financial Statements**
**December 31, 2004**

# Consolidated Balance Sheets

MACTEC, Inc. *(Dollars in thousands, except share amounts)*

| | December 31, 2004 | January 2, 2004 (Restated) |
|---|---|---|
| **Assets** | | |
| Cash and Cash Equivalents | $ 17,555 | $ 14,890 |
| Billed Fees Receivable, net | 68,418 | 64,860 |
| Unbilled Work in Progress | 26,624 | 46,218 |
| Other Receivables | 2,129 | 1,977 |
| Prepaid Expenses and Other Current Assets | 3,249 | 3,190 |
| Current Assets | 117,975 | 131,135 |
| Property and Equipment, net | 12,140 | 16,021 |
| Equity Investments | 134 | 138 |
| Goodwill | 86,900 | 87,284 |
| Intangible Assets, net | 34,935 | 38,793 |
| Other Assets, net | 20,279 | 18,138 |
| Total Assets | $ 272,363 | $ 291,509 |
| **Liabilities and Shareholders' Equity** | | |
| Accounts Payable | $ 27,571 | $ 29,349 |
| Billings in Excess of Costs and Fees Earned on Contracts in Progress | 21,239 | 23,935 |
| Accrued Payroll and Other Employee Benefits | 11,664 | 10,207 |
| Accrued Professional Liability Reserve | 7,221 | 8,882 |
| Other Accrued Expenses | 15,555 | 17,077 |
| Income Taxes Payable | 2,227 | 1,636 |
| Current Portion of Long-Term Debt | 7,074 | 6,780 |
| Current Liabilities | 92,551 | 97,866 |
| Long-Term Debt | 120,210 | 147,864 |
| Long-Term Liabilities | 23,265 | 20,063 |
| Class A Common Stock - $1 par value, 5,933,333 shares authorized, 189,584 shares Issued and Outstanding | 5,765 | 5,767 |
| Class B Common Stock - $1 par value, 66,667 shares authorized, 14,444 shares Issued and Outstanding | 433 | 433 |
| Preferred Stock - $.0001 par value, 3,500,000 shares authorized, 3,330,881 Issued and Outstanding | 9,993 | -- |
| Additional Paid-In Capital | 90,163 | 90,168 |
| Accumulated Deficit | (57,200) | (60,872) |
| Accumulated Other Comprehensive Loss | (12,817) | (9,780) |
| Total Shareholders' Equity | 36,337 | 25,716 |
| Total Liabilities and Shareholders' Equity | $ 272,363 | $ 291,509 |

See Accompanying Notes.

## Consolidated Statements of Operations

MACTEC, Inc. *(Dollars in thousands)*

| | Period Ended December 31, 2004 | Period Ended January 2, 2004 (Restated) |
|---|---|---|
| Gross Revenues | $ 432,665 | $ 426,781 |
| Less: Cost of Outside Services and Direct Expenses | 151,298 | 139,974 |
| Net Revenues | 281,367 | 286,807 |
| Cost of Net Revenues | 129,665 | 143,391 |
| Gross Profit | 151,702 | 143,416 |
| Indirect Costs and Expenses: | | |
| Payroll | 68,530 | 73,525 |
| Other Expenses | 51,543 | 55,836 |
| Depreciation and Amortization | 11,926 | 12,053 |
| Goodwill Impairment Charge | -- | 36,223 |
| Operating Income (Loss) | 19,703 | (34,221) |
| Other Income (Expense): | | |
| Interest Expense | (12,310) | (11,257) |
| Derivative Interest Expense | (315) | (309) |
| Deferred Financing Costs Amortization | (2,836) | (2,522) |
| Deferred Gain | 85 | -- |
| Other Income | 45 | 353 |
| Income (Loss) Before Income Taxes | 4,372 | (47,956) |
| Income Tax Provision | 700 | 132 |
| Net Income (Loss) | $ 3,672 | $ (48,088) |

See Accompanying Notes.

# Consolidated Statements of Shareholders' Equity

MACTEC, Inc. *(Dollars in thousands)*

| | Period Ended December 31, 2004 | Period Ended January 2, 2004 (Restated) |
|---|---|---|
| **Class A Common Stock, Balance at Beginning and End of Period** | | |
| Balance at Beginning of Period | $ 5,767 | $ 5,767 |
| Repurchase of Common Stock | (2) | -- |
| Balance at End of Period | 5,765 | 5,767 |
| **Class B Common Stock, Balance at Beginning and End of Period** | 433 | 433 |
| **Preferred Stock** | | |
| Balance at Beginning of Period | -- | -- |
| Issuance of Preferred Stock | 9,993 | -- |
| Balance at End of Period | 9,993 | -- |
| **Additional Paid-In Capital** | | |
| Balance at Beginning of Period | 90,168 | 87,142 |
| Issuance of Common Stock Warrants | -- | 3,026 |
| Repurchase of Common Stock | (5) | -- |
| Balance at End of Period | 90,163 | 90,168 |
| **Accumulated Deficit** | | |
| Balance at Beginning of Period | (60,872) | (12,784) |
| Net Income (Loss) | 3,672 | (48,088) |
| Balance at End of Period | (57,200) | (60,872) |
| **Accumulated Other Comprehensive Loss** | | |
| Balance at Beginning of Period | (9,780) | (6,537) |
| Minimum Pension Liability Adjustment | (3,037) | (3,243) |
| Balance at End of Period | (12,817) | (9,780) |
| **Total Shareholders' Equity** | $ 36,337 | $ 25,716 |

See Accompanying Notes.

## Consolidated Statements of Cash Flows

MACTEC, Inc. *(Dollars in thousands)*

| | Period Ended December 31, 2004 | Period Ended January 2, 2004 (Restated) |
|---|---|---|
| **Operating Activities:** | | |
| Net Income (Loss) | $ 3,672 | $ (48,088) |
| Adjustments to Reconcile Net Income (Loss) from Operations to Net Cash Provided by (Used in) Operating Activities: | | |
| Depreciation and Amortization | 12,806 | 13,029 |
| Goodwill Impairment Charge | -- | 36,223 |
| Common Stock Warrant Accretion | 512 | 341 |
| Financing Costs Amortization | 2,836 | 2,522 |
| Provision for Losses on Receivables | (25) | 1,611 |
| Deferred Gain | (85) | -- |
| Gain on Sale of Property and Equipment | (45) | (250) |
| Accrued Interest | 1,009 | -- |
| Stock Compensation | 109 | -- |
| Changes in Operating Working Capital Assets and Liabilities | 9,652 | 7,239 |
| Other, net | (1,127) | (4,375) |
| Net Cash Provided by Operating Activities | 29,314 | 8,252 |
| **Investing Activities:** | | |
| Purchases of Property and Equipment | (5,152) | (3,278) |
| Proceeds from Disposal of Property and Equipment | 1,885 | 1,387 |
| Net Cash Used In Investing Activities | (3,267) | (1,891) |
| **Financing Activities:** | | |
| Net Borrowings (Payments) on Revolving Line of Credit | (18,500) | 10,500 |
| Payment of Term Debt | (2,198) | (7,571) |
| Net Borrowings (Payments) on Supplemental Credit Facility | -- | 10,392 |
| Net Borrowings on Subordinated Debt | 2,799 | -- |
| Letter of Credit Deposit | -- | (5,063) |
| Purchase of Interest Rate Derivative | (488) | -- |
| Repurchase of Common Stock | (7) | -- |
| Debt Issuance Costs | (4,988) | (3,022) |
| Net Cash Provided by (Used In) Financing Activities | (23,382) | 5,236 |
| Increase in Cash and Cash Equivalents | 2,665 | 11,597 |
| Cash and Cash Equivalents at Beginning of Period | 14,890 | 3,293 |
| Cash and Cash Equivalents at End of Period | $ 17,555 | $ 14,890 |

See Accompanying Notes.

### 1. Basis of Presentation and Description of Business

On February 15, 2002 a group of investors purchased approximately 192,000 common shares of MACTEC, Inc. ("MACTEC") for $86,500 and MACTEC purchased substantially all of the remaining outstanding common shares for approximately $43,100. Also on February 15, 2002 MACTEC purchased all the outstanding common stock, cumulative convertible redeemable preferred stock and certain employee options to purchase common stock of Law Companies Group, Inc. ("Law") for approximately $86,000. Expenses of the MACTEC and Law transactions were approximately $4,686. In connection with these transactions, MACTEC entered into a Credit Agreement providing for a revolving line of credit facility of up to $35,000 and a term loan facility of $135,000 (see Debt). Each of the above transactions was conditioned upon all the transactions occurring. MACTEC completed the Law transaction to enhance their capabilities in engineering construction services, facilities engineering and environmental services. MACTEC, Inc. and Law Companies Group, Inc. are collectively referred to as the "Company".

The Company provides comprehensive environmental, design and consulting engineering, infrastructure and construction management services to governmental, commercial, and industrial entities generally in the United States. During 2004 and 2003, the Company derived approximately 11% and 15%, respectively, of gross fees from various agencies of the United States Government. At December 31, 2004 and January 2, 2004, receivables and unbilled work in progress from various agencies of the United States Government were $10,652 and $15,570, respectively.

The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions are eliminated. The period ended December 31, 2004 includes the period from January 3, 2004 to December 31, 2004. The period ended January 2, 2004 includes the period from December 28, 2002 to January 2, 2004.

### 2. Accounting Policies

**Restatement –** The 2003 financial statements have been restated to correct an error related to the receipt in January 2003 of a payroll tax refund of $1,763 from the Internal Revenue Service ("IRS") citing an overpayment of payroll taxes by the Company in 2001. In 2003, upon confirmation from the IRS, the Company recorded the refund as a reduction in payroll taxes. The Company, in conjunction with the IRS, has subsequently determined that the refund check was sent in error by the IRS and approximately $2,054, including interest, will be repaid in 2005.

The impact of the restatement to the Company's statement of operations for the year ended January 2, 2004, was a decrease to net income of $2,054, reflected as an increase to payroll expense of $1,763 and an increase to interest expense of $291. The restatement also increased Other Accrued Liabilities, Accumulated Deficit and Changes in Operating Working Capital Assets and Liabilities by $2,054.

**Use of Estimates -** The preparation of the financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

**Revenue Recognition -** In general, the Company recognizes revenue at the time services are performed. On cost-reimbursable contracts, revenue is recognized as costs are incurred, and includes applicable fees earned through the date services are provided. On fixed-price contracts, revenues are recorded using the percentage-of-completion method of accounting by relating contract costs incurred to date to total estimated contract costs at completion. Contract costs include both direct and indirect costs. Contract losses are provided for in their entirety in the period they become known, without regard to the percentage-of-completion. Some of the Company's contracts with the U.S. federal government, as well as certain contracts with commercial clients, provide that contract costs (including indirect costs) are subject to audit and adjustment. For all such contracts, revenues have been recorded based upon those amounts expected to be realized upon final settlement.

**Receivables and Unbilled Work in Progress -** Unbilled work in progress represents amounts earned under contracts in progress, but not yet billable under the terms of those contracts. These amounts become billable according to the contract terms which usually consider the passage of time, achievement of certain milestones, or completion of the project. Included in accounts receivable at December 31, 2004 and January 2, 2004 were contract retentions totaling $4,663 and $5,459, respectively. Substantially all unbilled receivables are billed and collected in the subsequent fiscal year. Allowances are recorded for receivables and unbilled work in progress when the Company determines collectibility is uncertain. Receivables and unbilled work in progress are written off once all means available to the Company to collect the amounts owed are exhausted. Billed fees receivable, net, at December 31, 2004 of $68,418 and at January 2, 2004 of $64,860 were net of allowances for doubtful accounts of $5,186 and $5,862, respectively.

**Cash Equivalents -** The Company considers all highly liquid investments with maturities of three months or less when purchased to be cash equivalents.

**Property and Equipment -** Property and equipment are stated at cost. Depreciation and amortization are provided over estimated useful lives using straight-line methods. Useful lives range as follows: buildings 30 years; equipment 3-6 and 10 years; furniture and fixtures 5-10 years; vehicles 3-6 years; and leasehold improvements utilizing the shorter of the lease term or the remaining useful life of the asset. Depreciation expense was $8,921 and $9,170 in 2004 and 2003, respectively. Long lived assets, including property and equipment and intangible assets with finite lives, are reviewed for impairment in accordance with SFAS No. 144 "*Accounting for the Impairment or Disposal of Long Lived Assets*" whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In analyzing potential impairment, the Company uses projections of future cash flows from the asset group. These projections are based on the Company's view of forecasted growth rates, anticipated future economic conditions, appropriate discount rates relative to risk, and estimates of residual values.

**Income Taxes -** The liability method is used in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the tax rates and laws that will be in effect when the differences are expected to reverse.

**Intangible Assets –** Intangible assets (contracts and customer relationships) are amortized over the average expected life which is estimated to be approximately ten years. Such amortization expense amounts to $3,858 for the period ended December 31, 2004 and $3,832 for the period ended January 2, 2004. Annual estimated amortization expense for each of the next five years is $3,832. Accumulated amortization approximated $11,043 and $7,185 at December 31, 2004 and January 2, 2004, respectively. Goodwill is an indefinite life asset and will not be amortized.

**Other Assets -** Included in Other Assets are debt financing costs which are amortized on a straight-line basis over the terms of the related agreement. Amortization expense approximated $2,836 and $2,522 for the periods ended December 31, 2004 and January 2, 2004, respectively. Accumulated amortization approximated $4,110 and $3,280 at December 31, 2004 and January 2, 2004, respectively. Costs related to internally developed software are accounted for in accordance with Statement of Financial Accounting Standards No. 86, "*Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed"*. Unamortized costs of $1,477 and $1,852 were recorded in Other Assets in 2004 and 2003, respectively. Software amortization of $848 and $976 were recorded in cost of outside services and direct expenses in 2004 and 2003, respectively. A cash escrow deposit of $5,063 related to a letter of credit is included in Other Assets at December 31, 2004 and January 2, 2004.

**New Pronouncements –** On December 16, 2004 the Financial Accounting Standards Board (FASB) issued SFAS 123 (revised 2004), Share-Based Payment, which is a revision of SFAS 123, *Accounting for Stock-Based Compensation.* SFAS 123(R) supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees,* and amends SFAS 95, *Statement of Cash Flows.* Generally, the approach in SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values. Pro forma disclosure is no longer an alternative.

SFAS 123(R) must be adopted no later than the first fiscal year beginning after December 15, 2005. Early adoption will be permitted in periods in which financial statements have not yet been issued. The Company expects to adopt SFAS 123(R) on January 1, 2006.

The Company currently accounts for its employee stock options in accordance with APB 25 (as described in Note 2) and SFAS 123(R) requires that the Company adopt the prospective method. Under the prospective method, the Company would continue to account for nonvested awards outstanding at the date of adoption of SFAS 123(R) in the same manner as they had been accounted for prior to adoption. All awards granted, modified, or settled after the date of adoption should be accounted for using the measurement, recognition and attribution provision of SFAS 123(R).

As permitted by SFAS 123, the Company currently accounts for share-based payments to employees using APB 25's intrinsic value method and, as such, generally recognizes no compensation cost for employee stock options. Accordingly, the adoption of SFAS 123(R)'s fair value method will have a significant impact on the Company's result of operations, although it will have no impact on the Company's overall financial position. The impact of adoption of SFAS 123(R) cannot be predicted at this time because it will depend on levels of share-based payments granted in the future. However, had the Company adopted SFAS 123(R) in prior periods, the impact of that standard would have approximated the impact of SFAS 123 as described below in the disclosure of pro forma net income in Note 2 to the consolidated financial statements. SFAS 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption. While the Company cannot estimate what those amounts will be in the future (because they depend on, among other things, when employees exercise stock options), the amount of operating cash flows recognized in prior periods for such excess tax deductions were zero in 2004 and 2003.

**Common Stock Reserved -** The Company has reserved 789,992 shares of common stock for issuance relative to employee stock option plans, other stock option plans, convertible securities, and common stock warrants related to the 2002 Stock Option/Stock Issuance Plan. There are an additional 54,246 shares reserved relative to the warrants issued in 2003 and 3,330,881 shares reserved relative to convertible preferred stock issued in 2004.

**Reclassification –** Certain prior year amounts have been classified to conform to the current year presentation.

**Stock Based Compensation -** The Company grants employees stock options for a fixed number of shares with an exercise price equal to the fair value of the shares at the date of grant. The Company has elected to account for stock option grants in accordance with APB Opinion No. 25, *Accounting for Stock Issued to Employees.*

Pro forma information regarding net income and earnings per share is required by SFAS 123, "*Accounting for Stock-Based Compensation*", and has been determined as if the Company had accounted for its employee stock options under the fair value method of that Statement. The fair value for these options was estimated at the date of grant using a Minimum Value option pricing model with the following weighted-average assumptions: risk-free interest rate with a range of 3.1% - 4.8%, dividend yield of 0%; and a weighted-average expected life of the option of 7.0 years.

*(Dollars in thousands, except share amounts)*

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting period. Had compensation cost been determined based on the fair value at the grant date consistent with the provisions of SFAS 123, the Company's net income (loss) would have been:

| | Period Ended December 31, 2004 | Period Ended January 2, 2004 (Restated) |
|---|---|---|
| Net income (loss), as reported | $ 3,672 | $ (48,088) |
| Compensation expense | (203) | (205) |
| Net income (loss), pro forma | $ 3,469 | $ (48,293) |

**3. Goodwill**

In accordance with Statement of Financial Accounting Standard No. 142 "*Goodwill and Other Intangible Assets*" this asset is reviewed at least annually for impairment, and is written down and charged to the results of operations in periods in which the recorded value of goodwill is more than its fair value. The Company tests for impairment by using a discounted cash flow approach. Based on the results of this test, the Company recognized an impairment charge of $36,223 in 2003, which is included in operating loss in the accompanying statements of operations. There was no impairment charge recorded in 2004.

**4. Comprehensive Loss**

Comprehensive loss for the periods ending December 31, 2004 and January 2, 2004 consist of the following:

| | Period Ended December 31, 2004 | Period Ended January 2, 2004 (Restated) |
|---|---|---|
| Net income (loss) | $ 3,672 | $ (48,088) |
| Minimum Pension Liability Adjustment | (3,037) | (3,243) |
| Comprehensive income (loss) | $ 635 | $ (51,331) |

*(Dollars in thousands, except share amounts)*

### 5. Property and Equipment

Property and Equipment are presented at cost less accumulated depreciation and are as follows:

| | December 31, 2004 | January 2, 2004 |
|---|---|---|
| Land and Buildings | $ 444 | $ 1,121 |
| Equipment | 35,753 | 31,722 |
| Furniture and Fixtures | 1,315 | 1,296 |
| Vehicles | 586 | 208 |
| Leasehold Improvements | 4,714 | 4,492 |
| | 42,812 | 38,839 |
| Less: Accumulated Depreciation | (30,672) | (22,818) |
| Total Net Property and Equipment | $ 12,140 | $ 16,021 |

### 6. Long-Term Debt

Debt obligations consist of the following at December 31, 2004 and January 2, 2004:

| | December 31, 2004 | January 2, 2004 |
|---|---|---|
| Revolving Lines of Credit | $ -- | $ 18,500 |
| Supplemental Facility | 400 | 10,392 |
| Term Debt, payable in quarterly installments | 73,375 | 125,110 |
| Subordinated Debt | 2,799 | -- |
| Term Debt, non-amortizing | 50,166 | -- |
| Note Payable for Capital Leases | 544 | 642 |
| Total Lines of Credit and Notes Payable | 127,284 | 154,644 |
| Less: Current Portion | 7,074 | 6,780 |
| Total Long-Term Debt | $ 120,210 | $ 147,864 |

Interest expense of $12,310 in 2004 includes $1,009 of accrued interest of which $531 has been reclassified to term debt, non-amortizing. Interest payments totaled $8,690 and $12,128 in 2004 and 2003, respectively.

On May 26, 2004, the Company amended and restated its credit agreement with various financial institutions (the "Credit Agreement"). The Credit Agreement provides a $20,000 revolving line of credit facility, an amortizing term loan facility of $76,629 and a non-amortizing term loan facility of $59,699. The Credit Agreement is secured by substantially all assets of the Company.

The revolving line of credit bears interest at either a base rate plus a margin of 2.75% or LIBOR plus a margin of 3.75%. The interest rate at December 31, 2004 was 7.50%. The Company's investors have guaranteed a portion of the revolving credit facility totaling $12,526. At December 31, 2004, there is no outstanding balance under the revolving line of credit. The revolving line of credit matures on January 31, 2009.

The amortizing term loan facility bears interest at either a base rate plus a margin of 3.00% or LIBOR plus a margin of 4.00%. The interest rate at December 31, 2004 was 6.04%. Amounts outstanding under the term loan are due as follows: $7,000 in 2005, $12,000 in 2006, $15,000 in 2007, $18,000 in 2008 and $21,375 thereafter. The term loan matures on January 31, 2009.

The non-amortizing term loan bears interest at 12%, comprised of 10% payable quarterly and 2% being deferred quarterly and added to the outstanding term loan balance. The outstanding principal balance is due on January 31, 2009.

*(Dollars in thousands, except share amounts)*

There are two capital leases which bear interest at 6.25% and 10.80%. Amounts outstanding under the leases are due as follows: $74 in 2005, $48 in 2006, $58 in 2007, $70 in 2008 and $294 thereafter. One lease matures on June 30, 2005 and the other lease matures December 31, 2011.

A letters of credit sub-facility, with a maximum outstanding balance of $15,000 is available under the revolving line of credit. Letters of credit outstanding at December 31, 2004 totaled $432. Letters of credit bear fees of 3.75% annually.

The Credit Agreement contains certain covenants which, among other things, require minimum earnings (as defined) and specify achievement of certain leverage, fixed charge and interest ratios.

Concurrent with the Credit Agreement closing, the Company's investors converted a supplemental credit facility with an outstanding balance of $9,993 to convertible preferred stock.

**7. Leases**

The Company leases certain office space, equipment, automobiles, and furniture under noncancellable operating leases. The following is a schedule of future minimum lease payments, net of noncancellable sublease income, required under those leases which have initial or remaining noncancellable terms of one year or more:

| | | |
|---|---|---|
| 2005 | $ | **15,462** |
| 2006 | | **12,375** |
| 2007 | | **8,354** |
| 2008 | | **6,137** |
| 2009 and thereafter | | **6,082** |
| | $ | **48,410** |

Rent expense, net of income from subleases, aggregated $19,201 and $18,270 in 2004 and 2003, respectively. Aggregate future minimum rents to be received under noncancellable subleases as of December 31, 2004 are $247.

In April 2004 the Company entered into a sale-leaseback transaction when it sold a building for $1,940. A gain of $1,276 was realized on the transaction and is being deferred over the 120 month life of the lease. The Company recognized $85 of the deferred gain in 2004. The Company is leasing back the space for 10 years. The schedule of future minimum lease payments above includes the lease payments for this space which consist of $190 for 2005, $195 for 2006, $200 for 2007, $206 for 2008, and $1,205 for 2009 and thereafter.

**8. Benefit Plans**

**Pension Plans**

A subsidiary of the Company has a noncontributory, defined benefit pension plan covering its United States employees over the age of 21 who were hired before March 28, 1996. The benefits are based on each eligible employee's years of service and compensation during the last ten years of employment. The Company uses a December 31 measurement date for its plan. A curtailment in the plan, which was effective March 28, 1997, ceased benefit accruals to vested participants on that date.

The Company's funding policy is to contribute amounts annually to the plan sufficient to meet minimum funding requirements as set forth in the Employee Retirement Income Security Act of 1974, plus additional amounts, if any, as may be determined to be appropriate by the Company's management.

*(Dollars in thousands, except share amounts)*

The following table sets forth the funded status and net prepaid pension asset (liability) recognized for the plan:

| | December 31, 2004 | January 2, 2004 |
|---|---|---|
| Benefit Obligation at End of Year | $ 68,199 | $ 60,997 |
| Fair Value of Plan Assets at End of Year | 52,368 | 48,348 |
| Funded Status | $ 15,831 | $ 12,649 |
| Accrued Liability | $ (15,831) | $ (12,649) |
| Accumulated Other Comprehensive Loss | 12,756 | 9,668 |
| Net Amount Recognized | $ (3,075) | $ (2,981) |

Benefits paid for the periods ended December 31, 2004 and January 2, 2004 were $1,567 and $1,194, respectively. Benefit cost for the periods ended December 31, 2004 and January 2, 2004 were $94 and $773, respectively.

The following table sets forth the components of net periodic benefit cost:

| | December 31, 2004 | January 2, 2004 |
|---|---|---|
| Interest Cost | $ 3,771 | $ 3,594 |
| Expected Return on Plan Assets | (4,054) | (2,822) |
| Recognized Actuarial Loss | 377 | -- |
| Net Periodic Benefit Cost | $ 94 | $ 772 |

Actuarial weighted average assumptions used to determine benefit obligations:

| | December 31, 2004 | January 2, 2004 |
|---|---|---|
| Discount Rate | 5.75% | 6.25% |
| Rate of Compensation Increase | N/A | N/A |

Actuarial weighted average assumptions used to determine net periodic benefit cost:

| | December 31, 2004 | January 2, 2004 |
|---|---|---|
| Discount Rate | 6.25% | 7.00% |
| Expected Long-Term Rate of Return on Plan Assets | 8.50% | 7.00% |

The expected long-term rate of return on plan assets was developed based on a capital markets model which uses expected class returns, variance and correlation assumptions. The expected class returns were developed starting with current treasury yields and then adding corporate bond spreads and equity risk premium to develop the return expectations for each. The expected class returns are forward-looking and are not developed by an examination of historical returns. The variance and correlation assumptions are also forward-looking. They take into account historical relationships, but are adjusted to reflect expected capital market trends.

*(Dollars in thousands, except share amounts)*

The Company's plan weighted average asset allocations are as follows:

| | December 31, 2004 | January 2, 2004 |
|---|---|---|
| Asset Category: | | |
| Equity Securities | **72%** | **70%** |
| Debt Securities | **15%** | **20%** |
| Real Estate | **--** | **--** |
| Other | **13%** | **10%** |
| Total | **100%** | **100%** |

The primary object for the assets of the Company is to promote the long-term growth of fund assets within the level of risk deemed acceptable for the Plan. This object is to be achieved through the establishment of an optimal asset structure and through the retention of quality investment management capable of meeting the specific performance goals.

By meeting these objectives, the Company seeks to achieve a high level of total investment return consistent with a prudent level of portfolio risk. The Company believes that the following standards are reasonable and achievable within the asset structure and investment guidelines.

Over rolling five year periods, the total portfolio compound annualized rate of return should:

- provide an annualized rate of return equal to or in excess of 7% - 8%
- exceed the return generated by an unmanaged index composed of the S&P 500 Stock Index, the Lehman Brothers Aggregate Bond Index, the Russell 2500 and the Europe, Australia & Far East (EAFE) International Stock Index in proportion to the target portfolio
- Maintain a risk level, as measured by the standard deviation of quarterly returns, which does not exceed that of the blended benchmark index by more than 33%.

Short term underperformance of these standards will not be a decisive factor in the evaluation of Plan and manager performance; however, significant short-term underperformance may make it unlikely that the Plan's longer term objectives will be achieved. Performance will be analyzed in the aggregate, by manager and by asset class to ascertain the likelihood of achieving the above goals in light of current market conditions as well as to determine the managers' specific strengths and weaknesses.

The asset structure should reflect a proper balance of the Plan's time horizon, needs for asset growth, liquidity and stability. The Company currently has a long term but finite investment horizon because the Plan is frozen. On a periodic basis, consideration should be given to modifying the target asset mix as necessary based on the Plan's changing needs. The target asset mix and acceptable tactical ranges associated with the achievement of the initial long term objectives of the Plan assets, is as follows:

*(Dollars in thousands, except share amounts)*

| Security Class | Tactical Range | Performance Measurement Goal |
|---|---|---|
| Equities: | **65% - 75%** | **70.0%** |
| Domestic Large Cap | **35% - 45%** | **40.0%** |
| Domestic Small/Mid Cap | **10% - 15%** | **12.5%** |
| International | **14% - 21%** | **17.5%** |
| Fixed Income | **25% - 35%** | **30.0%** |
| Cash Equivalents | **0% - 5%** | **--** |
| Total Pension Plan | | **100.0%** |

The target allocation provides reasonable assurance that the investment objectives can be achieved based on the historic relationships of asset class performance. Liquidity will be required only to meet payout needs.

The Company expects to contribute zero dollars to the Plan in 2005.

The expected benefit payments are as follows:

| Year | | Estimated Future Payments |
|---|---|---|
| 2005 | $ | **1,680** |
| 2006 | | **1,960** |
| 2007 | | **2,100** |
| 2008 | | **2,310** |
| 2009 | | **2,620** |
| 2010 - 2014 | | **18,010** |

The Company also has a defined contribution savings plan which qualifies under section 401(k) of the Internal Revenue Code, covering substantially all United States employees. The Company's matching contribution to the plan was $2,560 and $2,780 in 2004 and 2003, respectively.

**9. Shareholders' Equity**

**Common Stock**

On May 26, 2004, the Company completed a "1 for 30" reverse stock split. Accordingly, all share amounts have been retroactively adjusted to give effect to this change.

The Company currently has two authorized classes of common stock. Class A common stock has voting rights. On May 26, 2004, the Company increased the authorized shares of Class A common stock, $1.00 par value, to 5,933,333. At December 31, 2004, there were 189,584 shares outstanding and at January 2, 2004, there were 192,232 shares outstanding.

Class B common stock, $1.00 par value, has limited voting rights and can be converted to Class A common stock. The Company has authorized 66,667 shares of Class B common stock. At December 31, 2004 and January 2, 2004, 14,444 shares were outstanding.

Class C common stock was eliminated on May 26, 2004. It had no rights to dividends, voting privileges or conversion to other classes of stock; however, the Company was required to repurchase the stock from the holder upon either a subsidiary disposition or a sale of the Company. The Company had authorized one share of Class C common stock at $1.00 par value. At January 2, 2004 there were no shares outstanding.

**Preferred Stock**

Concurrent with the closing of the Credit Agreement dated May 26, 2004, the Company's investors converted debt held under a supplemental credit facility in the amount of $9,993 to Series A preferred stock. It has voting rights and shall vote with the holders of Class A common stock together as a single class. Preferred stock can be converted to Class A common stock at the option of the holder. The liquidation preference of each preferred share is three times the purchase price. The Company has authorized 3,500,000 shares with a $.0001 par value. At December 31, 2004, there were 3,330,881 shares outstanding.

**Stock Option Plan**

The Company has various stock option and incentive plans and is authorized under these plans to issue shares of the Company's Class A common stock to employees, directors and consultants. Options granted under the plans may be incentive stock options or nonqualified stock options. Stock purchase rights may also be granted under certain of the plans. Incentive stock options may only be granted to employees. The stock options vest ratably based on a variety of vesting schedules and expire ten years after the grant date.

*(Dollars in thousands, except share amounts)*

A summary of the Company's stock option activity and related information for the periods ended January 2, 2004 and December 31, 2004 follows:

| | 1999 Stock Option Plan (1) | 1999 Stock Incentive Plan (1) | 2000 Stock Option Plan (1) | 2002 Stock Incentive Plan (1) | 2002 Stock Option/Stock Issuance Plan |
|---|---|---|---|---|---|
| Shares issuable | 10,025 | 16,667 | 3,167 | 5,817 | 16,667 |
| Options outstanding – | | | | | |
| December 27, 2002 | 6,411 | 167 | 617 | 4,467 | 8,558 |
| Granted | -- | -- | -- | -- | 3,700 |
| Exercised | -- | -- | -- | -- | -- |
| Forfeited | (302) | -- | (17) | -- | (850) |
| Options outstanding – | | | | | |
| January 2, 2004 | 6,109 | 167 | 600 | 4,467 | 11,408 |
| Granted | -- | -- | -- | -- | 257,300 |
| Exercised | -- | -- | -- | -- | -- |
| Forfeited | (5,533) | (25) | (50) | -- | (30,700) |
| Options outstanding – | | | | | |
| December 31, 2004 | 576 | 142 | 550 | 4,467 | 238,008 |
| Exercisable – | | | | | |
| January 2, 2004 | 6,109 | 167 | 600 | 4,467 | 1,927 |
| December 31, 2004 | 576 | 142 | 550 | 4,467 | 4,194 |
| Weighted average fair value of options granted: | | | | | |
| January 2, 2004 | $ N/A | $ N/A | $ N/A | $ N/A | $ 55.50 |
| December 31, 2004 | $ N/A | $ N/A | $ N/A | $ N/A | $ .79 |
| Weighted average exercise price: | | | | | |
| Outstanding – | | | | | |
| December 27, 2002 | $ 174.00 | $ 300.00 | $ 300.00 | $ 149.10 | $ 450.00 |
| Granted | $ -- | $ -- | $ -- | $ -- | $ 275.70 |
| Exercised | $ -- | $ -- | $ -- | $ -- | $ -- |
| Forfeited | $ 174.00 | $ -- | $ 300.00 | $ 158.10 | $ 450.00 |
| Outstanding – | | | | | |
| January 2, 2004 | $ 174.00 | $ 300.00 | $ 300.00 | $ 149.10 | $ 393.00 |
| Exercisable – | | | | | |
| January 2, 2004 | $ 174.00 | $ 300.00 | $ 300.00 | $ 149.10 | $ 450.00 |
| Granted | $ -- | $ -- | $ -- | $ -- | $ 3.00 |
| Exercised | $ -- | $ -- | $ -- | $ -- | $ -- |
| Forfeited | $ 155.97 | $ 300.00 | $ 300.00 | $ -- | $ 7.37 |
| Outstanding – | | | | | |
| December 31, 2004 | $ 3.00 | $ 3.00 | $ 3.00 | $ 3.00 | $ 3.00 |
| Exercisable – | | | | | |
| December 31, 2004 | $ 3.00 | $ 3.00 | $ 3.00 | $ 3.00 | $ 3.00 |

(1) The stock options vested as of February 15, 2002 and expire ten years after the grant date.

In 2004 the Company repriced all outstanding stock options held by employees such that the options have an exercise price per share of $3.00. The weighted-average remaining contractual life of these options is 9.29 years.

*(Dollars in thousands, except share amounts)*

On March 31, 2004, the Board of Directors approved an amendment to increase the number of shares of common stock issuable under the 2002 Stock Option/Stock Issuance Plan to 1,028,009. The Company issued options totaling 257,300 in March 2004.

**Common Stock Warrants**

On April 3, 2003, in connection with the supplemental credit agreement, the Company issued common stock warrants to the supplemental credit agreement lenders to purchase up to an aggregate of 62,500 shares of Class A common stock for a period of ten years. The warrants have an exercise price per share of $225.00 and are exercisable through April 2013. The common stock warrants were valued at $3,026 based on the Black-Scholes valuation model. This debt discount was recorded as an increase in Additional Paid-In Capital and is being amortized to interest expense over the estimated life of the supplemental credit agreement. Amortization amounted to $512 and $341 in 2004 and 2003, respectively.

**10. Income Taxes**

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax liabilities include temporary differences related to goodwill amortization, prepaid expenses, and accounts receivable retention. Significant components of the Company's deferred tax assets include temporary differences related to depreciation, employee benefits, non-deductible reserves, and operating and capital loss carryforwards.

Deferred tax balances are as follows:

| | | **December 31, 2004** | | **January 2, 2004** |
|---|---|---|---|---|
| Assets | $ | **36,625** | $ | **39,601** |
| Liabilities | | **(26,348)** | | **(27,669)** |
| Valuation Allowance | | **(10,277)** | | **(11,932)** |
| Net Deferred Taxes | $ | **--** | $ | **--** |

Based on the available evidence as of December 31, 2004 and January 2, 2004, management concluded that the deferred tax assets should be reduced by a valuation allowance equal to the amount of the net deferred income tax assets.

At December 31, 2004 and January 2, 2004 the Company's federal and state net operating loss carryforwards for income tax purposes were approximately $46,634 and $53,567, respectively. If not utilized, these net operating loss carryforwards will begin to expire in 2021. Additionally, the utilization of a portion of these net operating loss carryforwards may be limited by IRC Section 382.

*(Dollars in thousands, except share amounts)*

A reconciliation of the statutory U.S. income tax rate to the Company's effective income tax rate is as follows:

| | Period Ended December 31, 2004 | Period Ended January 2, 2004 |
|---|---|---|
| Statutory U.S. Income Tax Rate | **34.0%** | **(34.0%)** |
| State Taxes, net of Federal Benefit | **11.6%** | **(3.6%)** |
| Permanent Differences Between Book and Taxable Income | **8.7%** | **0.4%** |
| Valuation Allowance | **(38.3%)** | **37.5%** |
| Effective Income Tax Rate | **16.0%** | **0.3%** |

Income tax refunds amounted to $379 and $132 in 2004 and 2003, respectively.

**11. Consolidated Statements of Cash Flows**

The change in operating working capital as shown in the Consolidated Statements of Cash Flows includes:

| | Period Ended December 31, 2004 | Period Ended January 2, 2004 (Restated) |
|---|---|---|
| Decrease (Increase) in: | | |
| Billed Fees Receivable | **$ (3,533)** | **$ (9,470)** |
| Unbilled Work in Progress | **19,594** | **19,131** |
| Other Current Assets | **106** | **11** |
| Increase (Decrease) in: | | |
| Accounts Payable and Accrued Expenses | **(3,819)** | **(7,759)** |
| Billings in Excess of Costs and Fees Earned on Contracts in Progress | **(2,696)** | **5,326** |
| Changes in Operating Working Capital Assets and Liabilities | **$ 9,652** | **$ 7,239** |

**12. Commitments and Contingencies**

The Company is a party to a number of lawsuits and claims arising in the ordinary course of its business. While the ultimate results of lawsuits or other proceedings against the Company cannot be predicted with certainty, management does not believe the ultimate costs of such actions, if any, in excess of amounts provided in the consolidated financial statements will have a material effect on the Company's consolidated financial position or results of operations.

**13. Financial Instruments**

The Company's financial instruments at December 31, 2004 and January 2, 2004 consist primarily of cash and cash equivalents, accounts receivable, accounts payable and loans payable. Due to the short maturities of the cash and cash equivalents, carrying amounts approximate the respective fair values. The carrying amount for loans payable approximates fair market value. Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash investments and trade accounts receivable. Concentrations of credit risk with respect to trade accounts receivable are limited due to the large number of entities comprising the Company's customer base. The Company performs ongoing credit evaluations of its customers' financial condition. Collateral is generally not required and credit losses have been within management's expectations.

The Company enters into certain derivative transactions designed to hedge risks associated with the interest related to its debt facility. The Company includes in operating results amounts received or paid when the underlying transaction settles. Derivatives are carried at fair value and are included in accrued liabilities or other assets on the balance sheet. Fair value is determined based on quotations from financial institutions. The Company does not enter into or hold derivatives for trading or speculative purposes. The Company does not designate the derivative instruments as hedges under Statement on Financial Accounting Standards No. 133, "*Accounting for Derivative Instruments and Hedging Activities,*" and accordingly the changes in valuation of the derivative instruments are recorded in the consolidated statement of operations.

At December 31, 2004, the Company was a party to two interest rate swap agreements which had been entered into to reduce the impact of changes in interest rates on a portion of its floating rate debt. The interest agreements are contracts to exchange variable rate for fixed rate interest payments periodically over the life of the agreements based upon the underlying notional amounts of the contracts. The net cash paid or received on these agreements is accrued and recognized as an adjustment to interest expense. In the event of early termination of interest rate swap agreements, any resulting gain or loss would be recognized in the statement of operations.

At December 31, 2004, the Company was party to two interest rate cap agreements which had been entered into to reduce the impact of changes in interest rates on a portion of its floating rate debt. Any cash received on these agreements are accrued and recognized as an adjustment to interest expense. In the event of early termination of the interest rate cap agreements, any resulting gain or loss would be recognized in the statement of operations.

As of December 31, 2004 and January 2, 2004, the Company had interest rate swap agreements with notional amounts aggregating $25,481 and $30,925, respectively for which it pays fixed interest rates between 6.7% and 6.8%. The swaps expire between May 31, 2005 and October 31, 2005.

As of December 31, 2004 and January 2, 2004, the Company had interest rate cap agreements with notional amounts aggregating $34,331 and $32,263, respectively with cap rates between 3.54% and 6.0%. The caps expire between April 30, 2005 and July 31, 2006.

The fair value of the swap and interest rate cap agreements totals $747 and $2,545 at December 31, 2004 and January 2, 2004, respectively, and is included in Long-Term Liabilities in the accompanying balance sheets.

## Report of Independent Auditors

The Board of Directors and Shareholders
MACTEC, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of MACTEC, Inc. and subsidiaries as of December 31, 2004 and January 2, 2004 (as restated), and the related consolidated statements of operations, shareholders' equity and cash flows for the periods ended December 31, 2004 and January 2, 2004 (as restated). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of MACTEC, Inc. and subsidiaries at December 31, 2004 and January 2, 2004, and the consolidated results of their operations and their cash flows for the periods then ended, in conformity with accounting principles generally accepted in the United States.

Ernst + Young LLP

Atlanta, Georgia
May 20, 2005

MACTEC, Inc.
August 19, 2005

Statement regarding MACTEC's stability and strength

MACTEC's stability and strength is best established by the following facts:

- In February 2002, the Company's equity partners invested in excess of $85 million in connection with the Company's recapitalization and merger. This provided a sound equity base for the Company. An additional $10 million of equity was invested in May 2004, further enhancing the Company's capitalization.

- In 2004, the Company generated in excess of $430 million in revenue from its network of approximately 100 offices. Earnings before interest, taxes, depreciation and amortization exceeded $31 million, were on target with budget expectations and reflect a much improved financial performance over 2003 and 2002.

- Working capital management at the Company is an ongoing component of operations. The Company's days sales outstanding at the end of 2004 stood at less than 66 days for both accounts receivable and work in progress. At December 2004, the Company's cash balances were $18 million, and net working capital was $25 million.

- The Company has a $158 million credit facility with its current lending group. The credit facility provides both term debt and revolving credit capacity sufficient to meet the growth needs of the business through 2008. The Company's $20 million revolving credit facility currently has only letters of credit of $0.4 million outstanding against it. The Company exceeded its debt reduction goals during 2004, ending the year with a much stronger balance sheet as it moves forward into 2005.

- The Company's current backlog totals $432 million of revenue. This equates to up to $650 million in gross revenue assuming a similar gross to net relationship as 2004.

The Company views its stability and strength primarily in terms of equity structure, revenue and profitability base, cash and working capital management, credit and financing capacity, and future revenue prospects. The Company believes that the facts outlined above indicate a firm financial base for current and future operations.